

Legislation
Chrono
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27 November 1985

MEMORANDUM FOR THE RECORD

SUBJECT: Tax Reform Legislation: Federal Annuity
Aspects and Prognosis for House Action

1. Finishing its work early on 22 November, the House Ways and Means Committee placed its stamp of approval on a comprehensive tax reform package. One provision of the bill concerns the method by which retirement annuities are taxed. Current tax treatment is governed by the "special 3 year basis recovery rule" under which annuities are not taxed until the amount of personal contribution is recovered. If the new legislation proposed by the Ways and Means Committee becomes law, a new method of taxation would apply.

2. This new rule would abolish the tax free period immediately and annuities would be taxed on a basis that is pro-rated over an actuarial assumption of the life expectancy of the annuity. While an annuitant would pay no more tax, the tax would begin with the first annuity check.

3. One substantive change made by the Committee in its marathon drafting session applies to the effective date of the law. Earlier versions of the bill included an effective date of 31 December 1985. Now the effective date for the annuity provision is 30 June 1986.

4. Even though the Ways and Means Committee completed action on the tax reform package, they must fulfill the technical requirement of voting on the report of the bill. Committee staff is still writing the report. It is expected that the report will be finished by 29 November, and the Committee will vote it out when they return on 3 December. Next, the Rules Committee will take action.

5. Depending on other business before the House during the remaining weeks of the first session - appropriations bills, conference reports, continuing resolutions - the tax reform bill will be taken up in the second or third week of December. However, revenue legislation (tax bills) ordinarily receive

preferred status on the floor of the House, and can automatically go to head of the head of the calendar for action. Most recently, news reports say that the House will not take up the bill until January.

6. After House action the bill will go to the Senate and be forwarded to the Senate Finance Committee to begin the process all over again. A warm reception is not expected in the Senate according to preliminary reports. Another school of thought believes that the tax package is an elaborate diversionary tactic to draw attention away from the federal deficit.

7. In summary, perhaps the best message to draw from all this is to avoid any precipitous action based upon the current provisions of the bill.




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